

## **BUDGET AND FINANCIAL POLICIES**

The City of Durham's budget and financial policies serve as the basis for developing the annual operating budget and the six-year Capital Improvement Program. The policies also serve as the basis for the City's overall financial management.

The Local Government Budget and Fiscal Control Act governs much of the activities that occur in budget preparation and execution. The City has placed other policies on itself voluntarily in order to address issues that are specific to Durham. Both types of policies are noted below.

### **Operating Budget Policies**

#### **State Statutes:**

- The City of Durham will operate under an annual balanced budget ordinance in which the sum of estimated net revenues and appropriated fund balance is equal to appropriations.
- By State Statute, the annual budget for all city funds, including enterprise funds, is prepared using the modified accrual basis of accounting. This basis of accounting recognizes revenues either when they are received in cash (such as licenses or fines) or when the collection of the amount can be reasonably estimated to be received in the near future (such as property taxes). Expenditures in a modified accrual system are generally recognized in the period in which goods or services are received or when a liability is incurred. Beginning with the FY 2001-02 Comprehensive Annual Financial Report, the City is accounting for its funds on both a full accrual and a modified accrual basis, in compliance with GASB 34.
- The General Fund has an officially adopted annual budget. The appropriations in the budget ordinance within the general fund are on a functional basis. Although General Statutes and generally accepted accounting principles do not require an annual balanced budget for the remaining funds, all governmental and enterprise funds have legally adopted balanced budgets.
- The City may establish and operate one or more internal service funds. At the same time that it adopts the budget ordinance, the City Council must approve a balanced financial plan for each internal service fund. A financial plan is balanced when estimated expenditures do not exceed estimated revenue.
- All grants received from the federal or state governments for operating or capital purposes will be recognized in separate grant project ordinances. A balanced grant project ordinance must be adopted prior to beginning the project. A grant project ordinance is balanced when estimated expenditures do not exceed estimated revenue. Information on each grant project ordinance is included in the Annual Budget.

- The City's budget ordinance will cover a fiscal year beginning July 1 and ending June 30. In order to have the budget ordinance approved by July 1, the Preliminary Budget, together with a budget message, will be submitted to the City Council no later than June 1.
- A public hearing will be held on the Preliminary Budget prior to adoption of the budget ordinance. Notice of this public hearing will be published in the Herald-Sun. This notice will also state that the Preliminary Budget has been submitted to the City Council and that a copy of the budget is available for review in the City Clerk's office.

#### City Policies:

- The City's budget will be presented in a program budget format that includes program summaries, current year accomplishments, proposed year budgetary changes, proposed strategies to be employed, and performance measures for each major program or service.
- The City's budget will include five-year revenue and appropriation projections for the General Fund and all major enterprise funds. These projections integrate the current financial picture with the outlook over the next five years.
- The City Manager has the authority to transfer funds within a departmental budget or within a functional category as set in the budget ordinance (i.e. from Fire to Police, within the same fund). The Budget and Management Services Department staff reviews all budget transfer requests and authorizes all transfers. All administrative budget transfers are documented by the Budget and Management Services Department and tracked in the City's general ledger.
- A budget ordinance amendment is necessary whenever a change is required in the original Budget Ordinance. Examples of such changes include changes to fund total or changes between functional category (i.e., moving funds from the non-departmental category to the Governance category in the General Fund). Any amendment must ensure that revenues and appropriations remain balanced. Budget ordinance amendments must be approved by the City Council. All budget ordinance amendments are documented by the City Clerk and the Budget and Management Services Department and tracked in the City's general ledger.

#### Fund Balance Levels

(City Policy, by resolution adopted June 21, 1999)

#### General Fund

- The City Council deems it desirable to achieve an undesignated fund balance level of 15% of adjusted appropriations. "Adjusted appropriations" shall equal total appropriations minus appropriations for debt service and transfers to other funds.

- Undesignated fund balance as a percentage of adjusted appropriations shall be no less than 12% of General Fund adjusted appropriations.
- Any fund balance between 12% and 15% of adjusted General Fund appropriations may be appropriated by the City Council, at its discretion, provided that the level of undesignated fund balance is not reduced below 12%.
- To limit the use of fund balance in the General Fund in any two-year budget preparation cycle, the maximum appropriation from fund balance shall be equivalent to a total of \$0.04 on the prevailing tax rate over the two-year planning period.
- Any fund balance beyond 15% of General Fund adjusted appropriations shall be transferred to the Capital Projects Fund. This transfer shall be made upon completion of the annual financial audit. It is the intent of the City Council to effect this transfer through an amendment to the subsequent year's Budget Ordinance.

### Capital Improvement Program

#### State Statutes

- The City will appropriate all funds for capital projects with a capital project ordinance in accordance with State Statutes.

#### City Policies

- The Capital Improvement Program (CIP) is a statement of the City of Durham's policy regarding long-range physical development. This plan is developed for a six-year period and is updated and revised annually. To be included in the CIP, each project must require a total expenditure of \$100,000 and have a useful life of at least six years.
- In all likelihood, the completion of capital projects will impact the departments' operating budgets as projects are completed and require maintenance and upkeep. Consequently, the impacts of capital projects on the annual operating budget are estimated and noted in the CIP.
- It is essential that CIP project proposals support, rather than contradict, plans and policies previously adopted by the City Council in order to coordinate and direct the physical development of the City. In evaluating each CIP proposal, particular attention is given to conformity of proposals with the Comprehensive Plan, the City's broadest overall policy and planning tool for managing growth.
- The CIP assumes the use of installment sales financing exclusively for either facilities that house City functions or facilities that are joint private-public ventures. This assumption is consistent with the stated goals of maintaining the existing infrastructure and providing City services in an effective and efficient manner.

- The CIP assumes the dedication of investment income toward general capital projects. By City Council resolution, all investment income derived by the General and Capital Projects Funds is dedicated to the Capital Projects Fund. This allows the City flexibility to accelerate or decelerate the spending schedules for capital projects funded on a pay-as-you-go basis depending on the rate of return received for the City's pooled cash. Due to the Governor's actions on state-shared revenues for FY 2001-02 and FY 2002-03 and the modest amount of investment income the City earns, investment income remains in the General Fund.
- The City will plan the use of water and sewer operating fund appropriations to capital projects on a multi-year basis to ensure that any future rate increases will be as level as possible throughout the planning period.

## **Investment Policy**

### **1. Policy**

It is the intent of the City of Durham to invest idle funds in accordance with North Carolina General Statutes (N.C.G.S.)159-30. The three chief objectives governing these guidelines are Safety of Principal, Liquidity, and yield, in that order.

### **2. Scope**

These investment guidelines apply to all the following funds in the City's cash pool (except debt and fiduciary funds): General Fund, Special Revenue Funds, Capital Projects Funds (unless prohibited by bond indentures), Enterprise Funds (unless prohibited by bond indentures), Internal Service Funds (with the exception of Risk related funds).

### **3. Definitions:**

*Short Term Portfolio:* Cash which is needed to meet the City's immediate and short-term payment obligations. Investment instruments in this portfolio will mature not later than one year after purchase.

*Intermediate Portfolio:* Cash which is needed to meet the City's obligations in the intermediate future (0-10 years). Investment instruments in this portfolio will mature not later than five years after purchase.

*Long Term Portfolio:* Cash which has been designated as an endowment to the Cemeteries and Transit Funds. Investment instruments in this portfolio will mature not later than twenty years after purchase.

### **4. Investment Priorities:**

Consistent with the three chief policy objectives (Safety, Liquidity and yield), all City funds covered by these guidelines, regardless of term, are invested with the following priorities:

- a. Safety - The investments will be undertaken in a manner that the principal amounts of the City's portfolio are preserved.
- b. Legality - The City's funds will be invested in accordance with State statutes and the

City's investment guidelines.

The City's *short term and intermediate portfolios* are invested under the following priorities:

- a. Liquidity - PRIMARY EMPHASIS - The City's funds will be invested in a manner that they are available when needed for disbursement without undue exposure to interest rate risk or maturity in accordance with the stated maximum maturity.
- b. Yield - SECONDARY EMPHASIS - The investments will be made in instruments that provide a fair market rate of return.

The City's *long term portfolio* is invested under the following priorities:

- a. Yield - PRIMARY EMPHASIS - The investments will be made in instruments that provide a fair market rate of return.
- b. Liquidity - SECONDARY EMPHASIS - The City's funds will be invested in a manner that they are available when needed for disbursement without undue exposure to market risk or maturity in accordance with the stated maximum maturity.

#### **5. Risk Tolerance:**

The City's objective is not to incur any losses through trading of securities. If a loss has to be taken to restructure or reposition a portfolio the action needs prior approval of the Finance Officer.

#### **6. Delegation of Authority:**

The Finance Officer, in accordance with N.C.G.S. 159-30, has the authority to invest unused city funds in any authorized investment instrument. Under the direction of Finance Officer, the Treasury Manager has the responsibility for the day to day management of City funds. The Finance Officer can also retain investment advisors on a contractual basis to manage the City's idle cash. Any investment advisor must be fully registered under the Investment Advisory Act of 1940.

#### **7. Oversight:**

All contractual investment advisors retained by the City will be under the oversight of an independent Investment Consultant. Both the consultants and the investment advisors will be under the oversight of the Treasury Manager, under the direction of the Finance Officer.

#### **8. Authorized Investments:**

The City has statutory authorization (NCGS 159-30) to invest its funds in the following:

- a. Certificates, notes, bonds or bills of the United States, or other obligations of the United States or its Agencies, where the same are fully guaranteed as to both principal and interest by the full faith and credit of the United States.
- b. Obligations of government-sponsored entities (Instrumentality) listed in NCGS 159-30 (c) (2).
- c. Obligations of State of North Carolina and bonds and notes of North Carolina local government or public authorities, subject to such restrictions as the Secretary of the Local Government Commission may impose.

- d. Certificates of Deposit of any North Carolina bank, secured in accordance with NCGS 159-31(b).
  - e. Prime quality Commercial paper rated the highest by one of the rating agencies and meeting the standards of NCGS 159-30 (c) (6).
  - f. Bankers Acceptance of a commercial bank. Either highest long term debt rating of at least one nationally recognized rating service, or the bank or its holding company is incorporated in North Carolina. In either event the security shall meet the standards of NCGS 159-30 (c) (7).
  - g. Mutual funds certified by the Local Government Commission (LGC) and meeting the standards of NCGS 159-30 (c) (8).
  - h. Repurchase agreements meeting the standards of NCGS 159-30 (c) (12).
  - i. If the City is to invest in Collateralized Mortgage Obligations (CMO) the instruments must: Pass the Federal Financial Instrumentality Examination Council (FFIEC) High Risk Security Test. Having underlying securities issued by a Federal Agency or Instrumentality. Must be an obligation of a federal agency or instrumentality as listed in NCGS 159-30(c)(2).
  - j. Other investments authorized by NCGS 159-30.
- A copy of the state investment statute (NCGS 159-30) is attached (Appendix A).

#### **9. Diversification:**

Investments of the City covered by these guidelines must be diversified to eliminate the risk of loss as a result of over-concentration of securities in a specific issuer, or a specific class of securities. The City will permit the investment of funds (excluding investments with maturity of less than 30 days) up to the following percentages for the various types of securities:

| <b>Type of Security</b>   | <b>Maximum Percentage</b>                    |
|---|--|
| U.S. Treasury Certificates, Bonds, Notes, and Bills. And Federal Agency issued obligations (8A) | 100% of Portfolio                            |
| United States Government Instrumentality (8B)   | 100% of Portfolio<br>30% per Instrumentality |
| Collateralized Mortgage Obligation (8I)   | 25% of Portfolio<br>20% per Security         |
| North Carolina State and Local Bonds I (8C)   | 50% of Portfolio                             |
| Certificates of Deposit (8D)  | 100% of Portfolio                            |
| Commercial Paper I (8E)   | 25% of Portfolio                             |
| Bankers Acceptance I (8F)   | 25% of Portfolio                             |
| LGC certified mutual funds (8G)   | 100% of Portfolio                            |
| Repurchase Agreements (8H)  | As required for overnight cash flow          |
| Continuous, discrete or European Callable securities (8A)                                       | 25% of Portfolio                             |

1. Within these classifications, no more than 20% of the Portfolio may be invested with a single issuer.
2. Does not apply to bond proceeds.

Note: Parenthetical references to section 8 of these guidelines.

#### **10. Maximum Maturities:**

*Short Term Portfolio:* The City will not invest in securities with a final maturity of more than one year from the date of purchase.

*Intermediate Term Portfolio:* The City will not invest in securities with a final maturity of more than five years from the date of purchase.

*Long Term Portfolio:* The City will not invest in securities with a final maturity of more than twenty years from the date of purchase.

Any exception from this will need the approval of the Finance Officer.

#### **11. Collateralization:**

The City requires collateralization for: Certificates of Deposit and repurchase (and reverse repurchase) agreements. In both cases the collateral must cover at least 105% of market value of principal and accrued interest.

Collateral will be held by an independent third party with whom the City has a custodial agreement. Safekeeping receipts must be supplied to the City evidencing ownership.

#### **12. Safekeeping and Custody:**

All security transactions, including collateral for repurchase agreements, entered into by the city or directed by asset managers on behalf of the city shall be conducted on a delivery-versus-payment (DVP) basis. Securities will be listed in the City's name if issued only in book entry form or held by a third party custodian designated by the Director of Finance and City Treasury Manager and evidenced by safekeeping receipts.

#### **13. Standards:**

Investments will be made according to the "Prudent Person" standard:

"Investments shall be made with judgment and care--under circumstances then prevailing--which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived." Officials and investment advisors making investment decisions in accordance with written procedures and the investment Guidelines and exercising due diligence will be relieved of personal responsibility for an individual security's credit risk or market price changes, provided deviations from expectations are reported in a timely fashion and appropriate action is taken to control adverse developments. Any person involved in the investment process shall refrain from personal business activities which could conflict with the proper execution of the investment program, or which could impair their ability to make impartial decisions. Furthermore any person involved in the investment program shall refrain from undertaking personal investment transactions with the same individual with whom business is conducted on behalf of the City. Investment consultants and advisors and employees of the City involved in the investment process, shall disclose any material or adverse financial interest that could be related to the performance of the City's

investment portfolio. City employees shall comply with the Code of Ethics of the City.

**14. Performance Standards:**

*Short Term Portfolio:* The City designates the three month Treasury Bill or Federal Agency overnight rate (whichever is higher) as the benchmark to ascertain if market yields are being achieved.

*Intermediate Term Portfolio:* The City designates the Lehman Intermediate Government Index net of cost as the benchmark for this portfolio.

*Long Term Portfolio:* The City designates the Lehman Long Term Government Bond Index net of cost as the benchmark for this portfolio.

**15. Reporting:**

The Treasury Manager will prepare and submit a monthly investment and cash forecasting report to the Finance Officer. In addition, a quarterly report will be submitted by the Finance Officer to the City Manager and City Council. The Treasury Manager is also responsible for providing investment and cash information to the City's external auditors.

**16. Authorized Financial Dealers and Institutions:**

All financial dealers and institutions that conduct investment transactions with the City will have on file with the City a Broker/Dealer Questionnaire (See Attachment 2). This questionnaire must be submitted prior to a firm being authorized to trade with the City, and annually thereafter in the month of June (does not apply to outside money managers.)

**17. Guideline Exceptions:**

Any deviation from the above guidelines must be confirmed in advance and in writing by the Finance Officer or Treasury Manager, under the direction of the Finance Officer.